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STATE FOR WHA/EPSC CORNEILLE, EB/ESC/IEC IZZO, S/P MANUEL, OES/STC  
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STATE PASS USTDAs for KMALONEY  
USAID FOR LAC/CEN KSIENKIEWICZ

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SUBJECT: Can Fish Oil Scale? Honduran Biodiesel Initiative Could Clash with U.S. Tax Incentives

REF: A. 2006 Tegucigalpa 2030

[¶](#)B. 2006 Tegucigalpa 1935

[¶](#)11. Summary: A GOH initiative to develop more energy independence may be in danger due to U.S. incentives that provide up to USD \$1 in tax credits for biodiesel refined in the U.S. The GOH plan to import over 1 million African Palms could conceivably meet about 30 percent of Honduras' diesel requirements, saving the country millions of dollars in fuel imports and providing a measure of control over its energy future. But if U.S. tax incentives convince U.S. companies to import the bulk of Honduras' African palm oil into the U.S., only small scale initiatives in Tilapia fish oil and pine nuts would be left to supply the Honduran domestic biodiesel market. Greater diversification in biodiesel feedstock may be the key to Honduras' energy future. End Summary.

AFRICAN PALMS SET TO TRIPLE

[¶](#)12. As reported reftels, the GOH has launched a plan to increase considerably the number of African Palms under cultivation with the intent to refine a significant portion of the harvested palm oil into biodiesel. The agrarian portion of the project is currently underway, with an agreement to import about 1.2 million African Palm oil plants from Malaysia having been signed last March 2006. The palms will be planted on approximately 200 thousand hectares of land on Honduras' humid north coast, almost tripling production from the 80 thousand hectares currently under cultivation.

[¶](#)13. Moises Starkman, the biodiesel czar appointed by President Jose Manuel "Mel" Zelaya Rosales to run the project, has stated consistently that job growth is the number one goal of the upstream agrarian project. With an estimated 1.5 jobs generated per hectare of land under African palm cultivation, the program could produce as many as 300 thousand new jobs. The palms would be cultivated in clusters, run primarily by cooperatives that would recruit new land owners to grow the palms while offering access to financing and training in return (details on this innovative financing scheme to be reported septel). In response to environmental concerns (fertilizer run-off and deforestation of existing trees, to name a few), Starkman offered to talk further with USAID reps to identify and address any concerns that might exist.

[¶](#)14. Currently several large processing facilities exist to convert the palm fruit into palm oil. One producer, Dinant corporation, has been exporting the bulk of the palm oil while using an increasing

amount as a blend in its consumer products (Note: Dinant holds the regional distribution license for Mazola products. End Note). Currently palm oil is Honduras' fifth largest export at about USD 56 million per year. Dinant has also been refining more and more palm oil into biodiesel - its processing plant's production is currently estimated at 6 thousand gallons of biodiesel a day, with a planned expansion to approximately 32 thousand a day by mid to late 2007.

#### THE CONSUMER TRIALS: ENERGY INDEPENDENCE FOR HONDURAS?

¶ 15. The projected increased level of available biodiesel will be vital for the downstream consumer trials now underway. Starkman initiated a limited trial of several hundred city buses that would run on a 5 percent biodiesel blend (Note: Diesel engines can normally run up to 20 percent biodiesel - B20 - without modifications. End Note). The trial was meant as much to educate the population that biodiesel does not harm car engines as it was to promote the use of an alternative fuel. Starkman's plan is to increase the percentage of diesel used in the trial to 20 percent by mid-2007.

¶ 16. A similar type of consumer trial sponsored by the mayor of Tegucigalpa has focused on overhauling the engines of about 60 city buses and using 100 percent biodiesel from the beginning. (Note: Blends containing over 20 percent biodiesel may corrode certain parts and clog the engine with residue from diesel usage. The engine needs to be cleaned and parts replaced to operate effectively with 100 percent biodiesel, particularly in the case of the aged bus fleet in Honduras. End Note). As opposed to Starkman's plan, the mayor's plan will source its fuel from Tilapia fish oil. Currently, Tilapia fish farms in the central Honduran lake of Yojoa produce approximately 1500 gallons of biodiesel per day.

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¶ 17. The consumer plan calls for a financing of about USD \$1500 per bus to overhaul the bus engines, then a software-driven payback mechanism that would recoup the financed amount over a period of time to be determined. The software would be connected to the biodiesel pump, charging the user a fraction more per tank and keeping a personalized record of expenditures, much like a debit card. The mayor's project qualified for a USTDA definitional mission to better clarify the project's business plan.

#### U.S. TAX INCENTIVES MAY CHANGE EQUATION

¶ 18. EconOff hosted several businessmen from Missouri-based biodiesel company American Biofuels October 25; their mission was to investigate the sourcing of biodiesel feedstock outside the U.S. Per the executives, the U.S. market for biodiesel is approximately 1 billion gallons a year, while supply is only about 200 million gallons a year (Note: Per other industry sources, the 1 billion gallon a year demand figure would constitute about 2% - B2 - of the 45 billion gallon a year diesel market in the U.S. If the blend was increased to B20, the biodiesel market could be as high as 9 billion gallons a year. End Note). Moreover, the current biodiesel feedstock and refinery projections place potential supply at only 700-800 million gallons in the next few years. The implication is that the demand for biodiesel will remain strong for the foreseeable future.

¶ 19. In order to help meet the demand and stimulate U.S. based refining capacity, a federal excise tax credit was issued in 2004 that equates to almost USD 1 dollar in credits per refined gallon of biodiesel (Note: H.R. 4520, or the American Jobs Creation Act of 2004, offers one US cent per percentage point of biodiesel blended with petroleum diesel for "first use" oils. End Note). The incentive is targeted towards developing feedstock and refining capacity in the U.S.; hence there is little incentive to source refined biodiesel outside the U.S. Consequently, companies interested in developing refining capacity, like American Biofuels, are actually looking internationally for potential sources of

biodiesel feedstock. Palm oil is one of the most efficient sources of biodiesel, and outside of Malaysia and Indonesia, one of the largest suppliers of African Palm oil is Honduras. (Note: Guatemala, at 40,000 hectares of African Palms under cultivation, has about half the current production of Honduras and offers a regional alternative. End Note).

¶10. The executives from American Biofuels were extremely interested in the developing African Palm oil industry in Honduras, and were close to closing a deal with one palm oil cooperative to help construct a palm oil processing facility and take all the finished palm oil that they could produce. The African Palm industry in Honduras includes between 5 to 6 cooperatives and 11 processing companies, but is dominated by Dinant corporation and its owner, Honduran businessman Miguel Facusse. Up to this point Facusse has been an ardent supporter of Starkman's African Palm-oil based consumer trial, and has committed to expanding his 6000 gallon a day biodiesel processing facility to over 30,000 by the end of 2007. With production improvements in the 3 other African Palm-based biodiesel refineries in Honduras, the supply of biodiesel could increase from the current 14,000 gallons a day to over 50,000 a day in the near future, providing the means to meet the demands of the consumer trial and potentially President Zelaya's goal of replacing 30 percent of imported diesel by the end of his term. (Note: Current diesel imports into Honduras are about 650,000 gallons per day, implying a total biodiesel production of around 200,000 gallons per day to reach this ambitious goal. End note.)

¶11. Starkman's trial, however, requires that biodiesel use be non-compulsory, in order to qualify for carbon-credits and allow the market to more efficiently select the type of fuel to be used. Consequently, there has been little mention of how and under what terms Starkman will contract the upstream biodiesel suppliers to provide sufficient biodiesel for expansion of his plan after the consumer trial ends. The American Biofuels executives, on the other hand, have started plans to develop a large scale African Palm oil-based refinery in the U.S. to capitalize on the tax credit and have spoken openly about signing contracts specifying volume commitments with their Honduran cooperative. (Comment: It is hard to believe that Facusse, faced with a monetary decision whether to refine the Palm oil into biodiesel or ship the feedstock African Palm oil to the U.S. would opt for any decision that does not maximize his profit. Given the heavy financial incentive to refine the palm oil in the U.S., the lack of import duties in the new CAFTA

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environment, and easy access to the major ports of Puerto Castillo and Puerto Cortes, it is easy to envision Facusse and the other producers shipping virtually their entire supply of African Palm oil to U.S. based refiners like American Biofuels. End Summary).

#### FISHY STORY: DIVERSIFICATION MAY ENSURE SUCCESS OF TRIALS

¶12. In light of the U.S. based refining incentives, Starkman's downstream consumer trial could be in jeopardy. However, the complementary consumer trial proposed by the mayor of Tegucigalpa may offer an intriguing alternative. The mayor's decision to source their biodiesel from Tilapia fish oil may guarantee at least a limited supply of biodiesel from a source other than African Palm oil. Moreover, recent initiatives to plant pine nut plants and construct biodiesel refineries in remote areas of central Honduras may give the consumer markets another option. That said, there are questions about the scalability and long-term sustainability of using such varied feedstocks. Per the American Biofuels executives, biodiesel refineries constructed at the scale necessary to meet the forecasted demand work most efficiently when optimized for one particular type of feedstock. EconOff and the mayor's office have made preliminary plans to showcase all the biodiesel initiatives to the USTDA consultant to determine the best way to ensure the survival of the consumer trials, and perhaps give some measure of energy independence to Honduras.

¶13. Comment: The lack of energy independence remains a hot-button political issue in Honduras and, with U.S. tax incentives positioned

to take most if not all of the promising African Palm oil production, diversification of feedstock may be the key to the survival of the nascent consumer trials. At issue is whether the current palm oil alternatives of Tilapia and pine nuts can scale sufficiently to offer a sustainable supply for the long term. Post hopes that the USTDA definitional mission will help marry the two consumer trial initiatives, and perhaps help determine the best way to ensure a stable supply for the domestic market. End Comment.

Williard